

Personal Financial Management - Lesson 6

Developing Your Spending Plan

ENABLING OBJECTIVES:

Upon completion of this lesson, students will be able to:

- 6.1 Prepare a spending plan
 - 6.1.1 Identify four critical areas of a spending plan
 - 6.1.2 Identify the optimum breakdown for total net income
 - 6.1.3 Explain the need for accuracy on the spending plan
- 6.2 List three ways to improve any spending plan.
- 6.3 Develop short- and long-term financial goals
- 6.4 Explain the difference between discretionary and non-discretionary spending
- 6.5 Define at least three ways to reduce discretionary spending
- 6.6 Identify different sources for help developing or revising a spending plan

REFERENCES:

- 1. OPNAVINST 1740.5A (Draft)
- 2. U.S. Navy's Personal Financial Management Standardized Curriculum (PERS 662)
- 3. OPNAVINST 1740.1 Fleet and Family Support Center Program
- 4. Command Financial Specialist Training Manual NAVPERS 15608C
- 5. www.lifelines2000.org
- 6. www.moneycentral.msn.com

SLIDES:

- 6-1 Lesson 6 Title Slide
- 6-2 Importance of a Plan
- 6-3 What Is a Spending Plan?
- 6-4 Why Have a Spending Plan?
- 6-5 Characteristics of a Spending Plan
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- 6-15 Savings Funds
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- 6-17 Increasing Discretionary Funds
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- 6-23 Effects of Compound Interest

CASE STUDIES:

None

VIDEO TAPES:

None

NOTES TO THE FACILITATOR:

The main points of this topic are:

Personal Financial Management - Lesson 6

Developing Your Spending Plan

- \$ The importance of developing a spending plan
 - \$ The formal steps necessary to develop a spending plan
 - \$ Benefits of establishing short and long term financial goals
 - \$ Techniques for reducing discretionary spending and benefits of doing so
- \$ Where to go for help

I. INTRODUCTION In this lesson we will discuss the importance of developing and following a sound spending plan. We will examine the components of a spending plan and talk about how to identify discretionary and non-discretionary spending. We will also talk about ways to reduce discretionary spending and the benefits of doing so. The last portion of the class will be devoted to actually preparing individual spending plans that can help you improve your financial health immediately.

A. A good game plan is key to success in any endeavor.

B. A personal spending plan is what my parents, and maybe yours, referred to as a budget. It's just a bit more sophisticated and looks further into the future.

SHOW SLIDE 6-1 LESSON 6 TITLE SLIDE

SHOW SLIDE 6-2 IMPORTANCE OF A GAME PLAN

SHOW SLIDE 6-3 WHAT IS A SPENDING PLAN?

- C. A good spending plan can improve your life in several ways.
1. Its most immediate contribution will be helping you live within your means.

Note to Facilitator

Ask the following question:
Remember we talked in the 1st lesson we talked about our goals. Why is a spending plan important to reaching those goals?

SHOW SLIDE 6-4 WHY HAVE A SPENDING PLAN?

| DISCUSSION POINT | RELATED INSTRUCTOR ACTIVITY |
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| <ul style="list-style-type: none"> 2. It can reduce stress that is often associated with financial problems. 3. It will help you establish and maintain a good credit history. 4. All of this will help you on the road to competence, confidence and achievement of personal goals. <p>D. A good spending plan is a guide and a servant, not a master. Here are some characteristics of a sound plan.</p> <ul style="list-style-type: none"> 1. A spending plan is a general guide. Everything does NOT have to be figured down to the penny. 2. It is unique to you and therefore reflects YOUR needs, wants, values, and goals. 3. To be practical and realistic, your plan should be based on your current income and expenses, but still allow for future possibilities. 4. Times and circumstances change, so your plan should be flexible enough to adapt. | <p>CLICK FOR BULLET</p> <p>CLICK FOR BULLET</p> <p>CLICK FOR BULLET</p> <p>SHOW SLIDE 6-5 CHARACTERISTICS OF A SPENDING PLAN</p> <p>CLICK FOR BULLET</p> <p>CLICK FOR BULLET</p> <p>CLICK FOR BULLET</p> |

5. A reasonable plan should allow for pleasures as well as necessities.

II. COMPONENTS OF A SPENDING PLAN. A spending plan is only one component of a Personal Financial Plan. There are three other parts that must be completed before preparing your spending plan.

- A. Current Net Worth. It's difficult to chart a course to a destination if you don't know where you are. That's the primary reason for determining your net worth -- which is nothing more than your total assets minus all your liabilities. Some of you may be surprised to learn how much you're worth when we do the exercise at the end of this class. You will also benefit from recognition of the fact that decreasing, or making a conscious decision not to increase, your liabilities directly and positively affects your net worth.
- B. Expenses. Determining what you have coming in each month and where it is going helps define the starting place for your spending plan. There are worksheets to help you make this determination.

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SHOW SLIDE 6-6 COMPONENTS OF A SPENDING PLAN

SHOW SLIDE 6-7 CURRENT NET WORTH

SHOW SLIDE 6-8 EXPENSES

C. Set Goals. This is where you identify your destinations. There are two categories of goals: short-term that can be accomplished in less than a year, and long-term that require a higher degree of commitment to your spending plan.

D. Steps to Goal Setting. Goal setting is accomplished in the steps shown here. We won't go into them in detail at this time since we will be using them in our upcoming exercise.

E. Spending Plan. After you have determined your net worth, identified current budget items, and set some goals, it will be time to develop your personal spending plan. We'll get you well down the road in the second hour of this class.

III. DEBT-TO-INCOME RATIO Part of our exercise will be to determine your debt-to-income ratio. This is simply the amount of your monthly debt payments divided by your monthly income, times one hundred. Mortgage payments, if you have them are not included as debt because real estate is considered an investment. Unless you were born with the proverbial silver spoon in your mouth, credit will be important to you for most of your life. The guidelines shown here should serve as a guide to the wise use of credit. It is so important that we'll devote an entire lesson to the subject later.

SHOW SLIDE 6-9 SETTING GOALS

SHOW SLIDE 6-10 GOAL SETTING STEPS

SHOW SLIDE 6-11 SPENDING PLAN

SHOW SLIDE 6-12 DEBT-TO-INCOME

IV. THE BIG PICTURE Any task is easier to accomplish if we understand why it's being undertaken, so let's look at a couple of well-established financial principles.

A. This financial pyramid shows the steps involved in successful management of personal finances. The top of the pyramid is the investment level. We'll devote an entire class to savings and investments. To stand the test of time, this pyramid, like any structure, must have a firm foundation -- in this case the two lower levels called management and savings. These levels involve managing your personal finances in a manner that will allow you to meet your obligations and begin to save for the future. How do you do this?

B. This chart shows a recommended breakdown of income distribution. Almost three quarters of your income will probably go for personal and family living expenses, and most people are likely to have some debt service, particularly early in life. However; Pay yourself first! Just like a creditor. Put away at least 10% of your paycheck each payday.

SHOW SLIDE 6-13 THE FINANCIAL PYRAMID

SHOW SLIDE 6-14 RECOMMENDED INCOME DISTRIBUTION

- C. The savings level of the pyramid was divided into three funds, shown here. The Reserve Fund is set aside for known or anticipated expenses such as vacations, holidays, and periodic insurance payments. It is also a good idea to build an Emergency Fund of one to three months pay for events like car repairs or replacing a major home appliance. With these two requirements met, establish a Goal-Getter Fund for things like an engagement ring, a car or a down payment on a home.

V. DISCRETIONARY VERSUS NON-DISCRETIONARY SPENDING The biggest obstacle most people, particularly young people, face in even starting to save for the future is that savings must be "paid" with discretionary funds. Non-discretionary spending is that about which you have no choice, namely living expenses and debt service - the bottom level of the financial pyramid. There are three things you can do to establish, or increase the amount of, discretionary funds available for savings. Non-discretionary spending are needs.

SHOW SLIDE 6-15 SAVINGS FUNDS**SHOW SLIDE 6-16 DISCRETIONARY VS NON-DISCRETIONARY SPENDING****Note to Facilitator**

Ask the following questions

Give me 4 examples of Non-discretionary spending.

Give me four examples of discretionary spending.

- A. One is to decrease your living expenses. This may be easier than you think. Forgo a dollar's worth of soda and snacks each workday, save the money, and you'll have \$250 in one year. Discretionary spending is wants.
- B. The second way to increase discretionary funds is to increase income. Obvious ways to do this are taking a second job or having a spouse who works. You might also want to check with your disbursing office to ensure your tax deductions are correct.
- C. Minimizing your debt load is the "fast track" to increased discretionary funds. Always shop for the lowest available interest rate and make more than minimum monthly payments when at all possible. Think long and hard before you acquire debt. As we said earlier, some debt is normal and expected, but that old concept of Delayed Gratification will pay more dividends than most of you can imagine at this stage of your life.

VI. WHO CAN HELP? If you think you are already in debt trouble, or if you need help in the future with any of the things we discuss in this course, don't be timid about seeking assistance from any of the sources shown here.

SHOW SLIDE 6-17 INCREASING DISCRETIONARY FUNDS

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SHOW SLIDE 6-18 SOURCES OF ASSISTANCE

VII. SPENDING PLAN EXERCISE We will now spend about an hour to get you started on preparing your personal spending plan. Remember that this plan is a living document, and I strongly encourage each of you to keep the materials we develop today and update them as your circumstances change.

SHOW SLIDE 6-19 PERSONAL SPENDING PLAN EXERCISE

NOTE TO FACILITATORS

Explain to students that they will be using the financial planning materials found in the student handouts. Talk the students through completion of the various forms. Check individual students work. Explain that the spending plans will be used in the car buying exercise the next day.

SHOW SLIDE 6-20 SAMPLE LES

VIII. SUMMARY. During this hour we talked about the advantages of a sound spending plan and steps for preparing your plan. We discussed some key economic concepts such as debt-to-income ratio, the financial pyramid, types of savings funds and the discretionary funds that are necessary to establish a savings program. We also identified ways to increase discretionary funds and sources of help for any of your financial concerns.

SHOW SLIDE 6-21 SUMMARY QUESTIONS**Summary Questions**

1. Who prepares a spending plan?
2. What are the four critical areas of a spending plan?
3. Name three ways to improve a spending plan?
4. Why do we need to set goals?
5. What are three ways we can reduce discretionary spending?

SHOW SLIDE 6-22 SUMMARY**SHOW SLIDE 6-23 EFFECTS OF COMPOUND INTEREST**

| DISCUSSION POINT | RELATED INSTRUCTOR ACTIVITY |
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